REPORT OF COMMITTEE ON CO-ORDINATION IN TAXATION

The Committee on Coördination in Taxation, appointed in 1916, which made a preliminary report in 1917, was reconstituted in 1918 by the appointment of Lawson Purdy, recently President of the Department of Taxes and Assessments of New York City, in place of Ogden L. Mills, then serving in France, and of Professor Henry W. Farnam, of the Department of Economics in Yale University, in place of Professor H. C. Adams of the University of Michigan, resigned, and it submits the following report as a basis for discussion.

With the close of the world war, problems of taxation press upon every country, and although the undestroyed wealth and undiminished earning power of our people make our burdens light, in comparison with other nations which must face vastly greater loads of debt with greatly decreased paying power, the time is opportune for a far-sighted and far-reaching review of our taxing methods, quite beyond what can be attempted in this report. Our improved financial system and methods, happily reformed in the nick of time, have enabled us to finance the huge expenses of the war without panic or serious privation, and although we already have a bonded debt reaching the unprecedented sum of $25,234,496,274, the fact that we have raised in the fiscal year 1919, as federal ordinary revenue alone, over $5,145,-882,546, largely by surtax on excess incomes and profits, shows that within a reasonable period, with well adjusted and continuously diminishing taxation, we can, if we so desire, pay off this huge debt, or accumulate an equivalent sinking fund, so that our surplus earnings may, within the present generation, be freed for further development of the resources of our country. But the readjustment of the political, social, economic, and financial conditions and methods, which the war has rendered inevitable in our own, as in other countries, and which must be interpreted largely in terms of taxation, call for the best thought of the best thinkers, such as the members of this Association, in shaping the future through present action.

A comprehensive view of this subject might include reports on taxation in other countries, as Great Britain, France, Germany, with particular reference to the pre-war taxation system of the early nineties, the Scandinavian countries, and the states of Australia and New Zealand, which have made so many radical experiments in taxation; and similar reports on the taxation systems of our several states, as related on the one side to federal, and on the other, to local taxes. Such reports would easily make a substantial volume, and no such work could be attempted by this Committee. The expected report of the Committee on War Taxation, headed by Professor Seligman, which is to include taxation in the belligerent countries, will cover much of the foreign ground, while a number of official or association reports and private publications during the present decade cover the last-

named field. This Committee, therefore, attempts only a summary of principles and suggestions.

Coördination in taxation means in this country, first of all, that federal, state, and local taxation should be related one to the other in practical systematization. It does not deal primarily with the merits of taxes, but chiefly with their relations one to another, whether these relations be of segregation or of concurrent jurisdiction. The first requisite for systematic taxation is a national budget and state and local budgets in which the needs of each taxing jurisdiction are clearly predetermined, that taxes may thus properly be determined and collected.

In relation to federal, state, and local taxes, there are three alternatives:

1. A unified system in which the subjects of taxation and the machinery of collection are the same, with allotment of the results to the several taxing divisions,—a system used by many of our states to cover state and local taxation, and used in some foreign countries to cover both national and local taxation, the rate being determined by the aggregated needs of the divisions participating.

2. A coördinated system under which: (1) certain subjects of taxation are alloted to one and certain others to another taxing division, *e.g.* in this country to the extent that imports are exclusively a national and land exclusively a state and local field of taxation, while local licenses are exclusively a source of local revenue; or (2) concurrent jurisdiction is arranged in the levying or collection of taxes in specified fields, *e.g.* inheritance taxes as between the nation and the states, and land taxes as between the state and its subdivisions.

3. A lack of system under which there is neither unification nor coordination but cris-cross confusion, as illustrated in this country by the separate levy of income taxes by the federal government and in certain states on different basis and in differing proportions.

In the consideration of national, state, and local taxes there are two principles which must be taken into consideration though they may not always coincide. The first is the equitable consideration, which requires that each unit of government—federal, state, or local—should draw its revenue from those sources appropriate to it, *i.e.* from those economic activities over which it has regular control or those to which it gives economic support. The second is the practical consideration which may often assign to the larger governmental unit taxes which, on the grounds of equity or law, could more logically be assigned to the smaller units. These considerations must be balanced, one with the other, through our schemes of taxation. In short, in seeking to obtain the revenue needed for our federal, state, or local government in the simplest, most efficient, and least objectionable way, we must make sure that economic laws and general principles are applied in such wise as may best fit in with our political and social order and the habits and thought of our people.

Coördination in taxation deals, also, with interstate taxation, *i.e.* in

relation to taxes within a state which interact or fail to interact with taxation in other states, and thus react within the state levying taxes, and with intrastate taxation *i.e.* in respect to the relation within the state of the several taxes or methods of taxation adopted by the individual state and, finally, with the relation of sate and local levy, collection, and distribution of taxes, into the details of which it is scarcely possible to venture in this report.

First among taxes naturally and almost necessarily national, are taxes upon exports and imports, based upon international trade and national markets, and for this reason national in character. The makers of our Constitution, recognizing that export taxes must be added to prices in foreign markets, thus putting us at disadvantage abroad, or deducted from prices in the home markets, thus putting us at disadvantage at home, forbade the use of export taxes by declaring (Article 1, Section IX, Sub-Section 5), in defining the powers of our government, that "no tax or duty shall be laid on articles exported from any state" and providing (Article 1, Section X, Sub-Section 2) that "no state shall, without the consent of the Congress, lay any impost or duty on imports or exports, except what may be absolutely necessary for executing its inspection laws, and the net produce of all duties and imposts, laid by any state on imports or exports, shall be for the use of the Treasury of the United States; and all such laws shall be subject to the revision and control of the Congress,"—a provision for inspection rather than taxation which no state has sought to exercise.

Import taxes, on the other hand, had been our chief source of national revenue previous to the adoption in 1913 of the 16th Amendment, abrogating the provision in the original Constitution (Article 1, Section IX, Sub-Section 4) that "no capitation or other direct tax shall be laid, unless in proportion to the census or enumeration hereinbefore directed to be taken" and to our war taxation of incomes and profits. The power to levy import taxes is specifically given to the Congress by the Constitution (Article 1, Section VIII) declaring that "the Congress shall have power to lay and collect taxes, duties and imposts and excises . . .; but all duties, imposts, and excises shall be uniform throughout the United States." In the fiscal year 1910, customs duties reached a maximum of $333,683,445, out of total ordinary receipts of $675,511,715, or nearly 50 per cent, sinking in the fiscal year 1919 to $178,813,704, out of total ordinary receipts of $5,145,882,546, or less than 4 per cent.

Excise taxes, specified in Article 1, Section VIII of the Constitution, above quoted, as a source of national revenue, but not denied to the states, had been normally, previous to 1910, when the special tax on corporations was first levied, the second greatest source of federal revenue, reaching in 1907, on spirits and liquors, tobacco, oleomargarine and miscellaneous sources, a total of $269,666,773, out of total ordinary receipts of $663,125,660,—the largest federal receipts previous to 1910. Under war taxation, excise taxes on spirits and liquors, tobacco, and oleomargarine rose in 1919 to $691,845,777, out of total

federal ordinary receipts of \$5,145,882,546, to which were added the receipts from the numberless sources specified in the war revenue legislation of 1917-18, chiefly of excise character. Excise taxes, defined by Webster as primarily "an inland duty or impost operating as an indirect tax on the consumer, levied upon certain specified articles, grown or manufactured, in the country," though possibly inclusive also of taxes "upon licenses to pursue certain trades and deal in certain commodities" as well as "certain direct taxes," have been levied by the federal government chiefly in this primary sense upon manufacture or growth of spirits and liquors, tobacco, and oleomargarine. Such taxes are desirably federal rather than state or local, as otherwise the manufacture of spirits or liquors and growth of tobacco would be driven or induced from one state to another by state taxes varying in different states, and possibly varying in the same state, from year to year, as an inducement to the immigration of such industries from other states. In any proper system of coördination of taxes, excise taxes at the process of growth or primary manufacture should be confined to federal use, for the reason stated; while, if utilized for state and local purposes, they should be confined to distribution or consumption of such commodities, as in the excise taxes on liquors, which, previous to prohibition, constituted so large a portion of the revenue of New York.

Income taxes, forbidden to the federal government by the original Constitution, as above quoted, became a possible source of national revenue on the adoption in 1913 of the 16th Amendment, providing that "the Congress shall have power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several states, and without regard to any census or enumeration." Taxes on personal incomes were first levied by the federal government within the year 1913, to the extent of \$28,253,535. In the year 1917, personal income and profit taxes reached \$675,249,450; partnership taxes, \$103,887,984; corporation income taxes, \$503,698,029; and corporation excess profits taxes, \$1,638,747,740; aggregating for income and excess profits taxes \$2,921,583,203, and the Treasury returns for the succeeding years, closely estimated, but not yet officially verified are, for 1918, individual income taxes, \$1,432,000,000; corporation income taxes, \$775,000,000; and excess profits taxes, \$2,500,000,000, in a total of \$4,707,000,000; and, for 1919, individual income taxes, \$1,290,000,000; corporation income taxes, \$510,000,000; and excess profits taxes, \$1,250,000,000, in a total of \$3,050,000,000. The federal income tax system, under the present law, lacks coördination within itself, for it treats partnerships and corporations doing similar and competitive business on absolutely different bases, so that under some circumstances, partnerships, and under others, corporations, are advantaged or disadvantaged, respectively. Also, corporations are subjected to the excess profits tax, as a complement to the income tax, to an amount reaching in some cases as high as 81½ per cent of returns in the highest zone. It has been proposed (by Professor T. S. Adams) that the excess profits tax should take the form

of a business tax on all business, corporate or other, on a standard basis, with a surtax on undivided profits.

Income taxes had long ago been adopted by many states, but superimposed upon instead of replacing other taxes in complicated taxing methods, they proved unworkable, the maximum return in any state being $122,056 in Virginia in 1907, and fell into disrepute, although some southern states still nominally retain them in the old form. Wisconsin pioneered the way to a better method in its law of 1911, levying a tax at reasonable progressive rates on the incomes of individuals, firms, and corporations (except transportation, public utility, banking, and like corporations taxed by other methods), exempting from taxation intangible property, farm machinery, and household goods, and providing an adequate force of local assessors under control of the state tax commission. It seems worth while to recount briefly the development of this tax.

In 1904 the platforms of all political parties favored an income tax, and a constitutional amendment, accepted in 1907 by unanimous vote of the Senate and with but one dissenting vote in the Assembly, was in 1908 adopted by the people, 85,696 to 37,729. The amendment added a provision that "Taxes may also be imposed on incomes, privileges and occupations, which taxes may be graduated and progressive, and reasonable exemptions may be provided." When the necessary bill was drafted by a recess committee, opposition developed, so that the Senate vote was 15 to 14 when in 1911 it became law, to be effective January 1, 1912, for incomes of 1911. To test the constitutionality of the law, the original jurisdiction of the Wisconsin Supreme Court was invoked and the state intervened through a suit against its own officials, in which the decision of January 9, 1912, supported the law on all points at issue, although the questions of the right to tax residents on all income, and non-residents, without exemption, on incomes within the state only, were not raised. The law exempted $800 for an individual or $1200 for husband and wife, with $200 additional for each child or dependent, but made no exemption for non-residents or corporations, the socialist vote in the legislature requiring increase to this point, although it was pointed out that in forty European states and territories the exemption approximated $150 only. The salient feature of the law was "diffused progression," with a tax of 1 per cent on the first taxable $1000, 1/4 of one per cent additional for each $1000, up to 2 per cent on the fifth $1000, thence 1/2 of 1 per cent additional on each $1000, up to 5 1/2 per cent on the twelfth $1000, and 6 per cent on the excess above $12,000, a succession of thirteen steps, comparable with seventeen to thirty-one grades in the German states and twenty-nine in the Swedish law, which produced an average of 1 1/2 per cent on a $5000 taxable income, or 3 per cent on $12,000 taxable income. Corporation taxes, under the original law, were based on the percentage of income to the plant or property producing it, at 1/2 of 1 per cent of an income within 1 per cent, and 1/2 of 1 per cent on each additional 1 per cent of income, up to

6 per cent on a taxable income of 12 per cent or more. This feature had precedent in a Georgia law of 1863 and in a Swedish law of 1910. The original law included under income the rental value of the house of an owner-occupier. An attempt at repeal was made a party issue, Republicans for the law, Democrats for repeal, in 1912, but the attack failed, although the state presidential vote was Democratic.

The law has been amended in the successive legislatures of 1913, 1915, 1917, and 1919 in many respects. Corporation taxes were changed in 1913, and now run from 2 per cent on the first $1000 up to $7000, where the rate is 6 per cent on the seventh $1000 and over. By an amendment of 1917 the rental value of the house of an owner-occupier was no longer counted as income.

The system avoids double taxation of personal property by permitting tax receipts for such to be used as offset or cash in payment of income taxes. The non-resident is taxed on income from property located and business transacted in the state. This includes income from rentals and royalties, but does not include income from intangible property or from personal services. The tax on corporations doing interstate business is based on the proportion of income earned within the state to the plant or property and total business within the state. This seemingly complicated plan has proved workable, because it is administered by special officials through the state directly under control of the state tax commission, and it has resulted in a revenue greatly above that from personal property previously taxed, reaching in the first year $3,482,145, or, less offset, $1,631,413 cash, and climbing steadily up to $9,482,595, or, less offset, $6,161,067 in 1917 and $11,830,142 in 1918, further figures being yet unavailable. Of the total returns, 10 per cent is withheld by the state to cover administrative costs, 20 per cent goes to counties and 70 per cent to towns, thus coördinating state and local taxation. This proportion was found to give certain towns an undue and unnecessary amount, and an amendment provided that in such cases the surplus should be redistributed on the basis of school population. The state provides separate blanks for the several classes of taxpayers, of course not related with the federal blanks later in force.

Oklahoma passed in 1915 a law modeled on the Wisconsin law, but since much amended.

Missouri in 1917 adopted a general income tax on individuals and corporations, with a personal exemption of $3000, or $4000 for husband and wife, at the rate of ½ of 1 per cent, basing the method on the federal form, and thus setting to other states an example of coördination with federal methods.

Massachusetts, in 1916, replaced that part of its general property tax covering intangibles by an income tax on incomes from intangible property, retaining the tax on professional and like incomes, which had been in vogue for nearly three centuries, and also including a tax of 3 per cent on sales of intangible property, leaving the property tax upon tangible property. The federal tax return is available to some

extent for Massachusetts' purposes. The rate is a flat 6 per cent on incomes from intangibles; incomes within $600 being allowed an exemption on intangibles of $300; and the business or profession tax is at $1\frac{1}{2}$ per cent, with an exemption of $2000, plus a possible further exemption of $1000 for a married man, children or dependents. The tax became effective in 1917 and, under the authority of the state tax commission, with district assessors for incomes, has produced substantially increased revenue, partly by bringing to light intangible properties which had hitherto escaped. Connecticut has no personal income tax, but in 1915 adopted an income tax on miscellaneous business corporations, superimposed upon federal tax, at 2 per cent, and required each corporation to file with the state tax commission a copy of its federal report, which process seems to have involved not a little confusion in the correspondence of corporations regarding federal and state taxes, respectively.

Virginia in 1918 amended its derelict income tax law, adopting a partial income tax, following the example of Massachusetts. Delaware in 1917 adopted an income tax law, taxing natural persons at the rate of 1 per cent on incomes over $1000.

New York passed a personal income tax law, effective May 14, 1919, which levies taxes, with exemption of $1000 for single and $2000 for married persons, and $200 additional for each dependent minor or incapable, at the rate of 1 per cent on the first $10,000, 2 per cent above, and 3 per cent on excess beyond $50,000. The schedules and deductions are, in some respects, the same as in federal income taxes, but in other respects different. The tax is also levied on non-residents, but inadvertently, at the flat rate of 2 per cent originally embodied in the bill, to the extent of their income earned within the state, for the purpose of obtaining revenue from New Jersey and other suburbanites who do business or practice professions within New York, but with rateable deductions, on account of taxes paid at residence, provided the state of residence makes reciprocal provision. By Section 363, referring to a non-resident: "The controller shall credit the amount of income tax payable by him under this article with such proportion of the tax so payable by him to the state or country where he resides as his income subject to taxation under this article bears to his entire income upon which the tax so payable to such other state or country was imposed." This scheme to tax non-residents and avoid double taxation is an experiment which will be watched with interest.

Alabama adopted in the summer of 1919 an up-to-date income tax law, following the New York pattern, and New Mexico and North Dakota have also adopted income tax laws in the present year.

These methods of taxing personal incomes by the federal government and by the several states are so diverse in basis and rate, as well as so recent, as to make analysis of results and effects difficult. It seems assured that income taxes will continue to be levied by the federal government, as a principal source of revenue, and that more states will substitute this method, in whole or in part, for the general property

tax. This should involve coördination, first, between the federal and state governments, and secondly, between the several states. The federal basis and schedule should be so simplified as to avoid the enormous and wasteful expense both on individuals and business corporations and on the federal government in connection with accounting and auditing, and these should be adopted by the several states as the foundation of any state method of taxing personal income. The aggregate should not be so high as to make the taxes excessive. Unless a useful method and rate are adopted by the several states, this form of taxes peculiarly invites change of residence from one state to another, even if the New York device as to non-residents proves workable. It would seem that if states impose an income tax, the basis of the tax should be as nearly as practicable the same as that employed by the federal government. In the case of persons receiving all their income from sources within their own state, the statement made to the state might be the same as the statement made to the United States. When part of the income is derived from two or more states, the simplest possible basis of apportionment should be adopted, so that the statement of total income may be the same for the states as for the nation, making the two returns identical, except that the tax to be paid to the state would be reduced in accordance with the method of apportionment adopted. In any event, the returns to federal and state authorities should be accessible to the taxing officers of both jurisdictions.

Corporation taxes are the most pressing and perplexing problem in our taxation, for the reasons that so vast a proportion of our business is done by corporations; that they may be taxed in the state of incorporation or nominal place of business, at the actual chief office elsewhere, in the state or states in which manufacturing plants are situated, and in the states in which business is done and income earned; that they afford no simple starting point for taxing, as in personal income; that their capitalization bears no necessary relation to their property, output or income; that the property at the base of their business may be intangibles, as newspapers, copyrights, patents, etc., as well as physical plant; that the practice in the several states and within states is confusing to the uttermost; and that the methods of taxation are multiform. Corporation taxes may be in the shape of licenses, or franchise tax, organization tax, stock transfer tax, tax on capital, on gross receipts or net income or dividends, or ad valorem on plant or value of property productive of income. Some of the states, notably Maine, Delaware, and formerly New Jersey, have made organization easy and loose, that revenue may later be squeezed from corporations, and the squeezing of corporations has been a favorite pastime of legislatures. No tax founded on nominal capitalization is just, because some corporations of long standing have held to their small original capitalization and saved earnings to add to actual capital till the original may be increased many fold, while in others the capitalization is largely water, and in some cases stock has no nominal par value, but represents a fractional part of the total value of the

corporation, a system definitely recognized in the laws of New York and certain other states. It is impracticable to schedule or generalize the multiform method and rates used in the different states, many of which have different forms of taxation for different classes of corporations.

As the federal government has made corporation taxes on an income and profit basis an essential feature of the present revenue methods, and as the states are not likely to yield this field of taxation, the sensible plan for coördination, as illustrated in the trend of legislation in some of the states, is to provide for state returns as nearly as practicable in the same form as the federal return, with as simple as possible an apportionment to avoid an unfair tax upon the corporation in any one state, superimposed upon the federal corporation tax, which should itself be simplified, so that it should not be necessary for a corporation to require a special staff of bookkeepers or a tax expert to meet federal and state requirements. The New York method was probably adopted in order to conform as nearly as might be to previous practice. Simplicity and ease of determination may excuse or even justify some theoretical injustice. The ascertainment of values in determining net income or profit of a corporation in proportion to investment is of course difficult, but perhaps not more difficult than other questions of assessment, and the taxation in each state on business done within the state should prevent double taxation and such intricate and confusing inter-relation between different states as the New York law involves.

It should be recognized, as the Secretary of the Treasury has pointed out, that excessive profits taxes result in evasion of taxation and loss of revenue, and probably the limit for the highest taxation in the zone of largest income or profit should be not more than 50 per cent, inclusive both of federal and state taxation. The excessive rate recently in vogue has induced reckless and wasteful expenditure on the part of corporations, as, for instance, in the advertising of automobiles, and one instance is cited in another field, where $300,000 is said to have been spent in advertising because the corporation was advised that under the excessive profits tax the actual net cost to the corporation would be within $40,000.

The income tax on corporations invites serious objection, in so far as it fails to recognize the extreme range of incomes on the part of corporations which have a few thousand dollars capital and those which require millions of capital, and though producing seemingly enormous returns, have, in fact, a relatively low return on investment. Several states have adopted the method of taxing gross earnings, which raises a similar objection, but has the merit of simplicity. The alternative suggestion has been made (by Lawson Purdy) that if tax exemption of securities can ultimately be modified or abandoned, a tax on dividends and bond interest might be feasible and just, since the use of earnings for increasing productive capital, instead of their diffusion in dividends, has economic value, if it is not worked to avoid taxation.

Inheritance taxes had not been levied, except at the time of the Spanish-American war, by the national government previous to the law of 1916, which has been amended in successive years. These laws have levied a tax rising from 1 per cent to 2 per cent, and again dropping to 1 per cent, on estates not exceeding $50,000, and taxed the excess without regard to consanguinity, from 2 per cent on excess above $50,000 to 25 per cent on excess above $10,000,000, producing in the year 1919 $82,029,983 of revenue. Inheritance taxes had for many years been levied by most of the states, five southern states excepted, varying in proportion to estate values and to degrees of consanguinity. The older eastern states are simple and conservative in these taxes, bequests in New York to lineals being taxed above $10,000, from 1 per cent on $25,000, up to 4 per cent above $100,000; to near collaterals, beyond $500, 2 per cent on $25,000, up to 5 per cent above $100,000; to others more remote, above $500, 5 per cent on $25,000, up to 8 per cent above $100,000. California, at the other extreme, developed a complicated and very high levy, bequests to lineals beyond $24,000 exemption to widow or minor child, or $10,000 to others, being taxed from 1 per cent until $25,000, up to 15 per cent above $1,000,000; to near collaterals, above $2,000, from 3 per cent until $25,000, up to 25 per cent above $1,000,000; to farther collaterals above $1,000, from 4 per cent until $25,000 up to 30 per cent above $1,000,000; to more remote beneficiaries above $500, from 5 per cent until $25,000, up to 30 per cent above $500,000. Wisconsin pursues a middle course, taxing bequests, with the exemption varying from $10,000 for widows to $100 for strangers, to lineals, 1 per cent; to near collaterals, 1½ per cent; farther collaterals, 3 per cent; more remote of kin, 4 per cent; other beneficiaries, 5 per cent until $25,000, these rates being multiplied from ½ times up to 3 times on estates above $5,000,000.

The remarks regarding income taxes are in large measure applicable to inheritance taxes, although there is less likelihood that a citizen will change his residence because of excessive inheritance taxes. Nevertheless, evidence is not lacking that this effect is produced. Great fortunes are not usually rolled up until the later years of life, when death is more in sight, and the exodus of California millionaires to eastern residence may partly result from the very high inheritance taxes of that state. While in one sense the inheritance tax is preferably federal, in that uniformity throughout the states is desirable, there is no substantial reason against its use by the states, and a compromise plan by which the federal tax would be limited to fortunes above $50,000 seems not an unreasonable compromise. However desirable on general principles, a single levy is preferable from a single source. Another plan proposed is federal taxation solely, with return of receipts in proportion to the several states, on an equitable basis, which would avoid the most serious evil of the present method by which inheritances may be taxed in multiple by two or more states. Another possible compromise is that the federal inheritance tax should be limited to intangibles, while the several states would levy such tax upon realty and other tangibles in situ within the state. On the other

hand, inheritance taxes have so largely been left to the states that many consider that this source of taxes might fairly after the war period, be relegated by the nation to the states, provided that proper precautions are taken by each state against double taxation.

Land, which in these United States is under the sole sovereignty of the sovereign state instead of the federated nation, has naturally formed a chief source of revenue in state taxation, and under the "Henry George" single tax proposal would form, if sufficing, the sole source of revenue for all purposes. Land, usually with improvements thereon, has been in general subject to property tax, in this country, though in other countries the practice or tendency has been to tax land through income. From this tendency there was a natural reaction when the development of cities increased the value of unproductive land, freed from taxation, in the hands of speculators. Realty is the form of property tax for state revenue on which practically all authorities agree, though with serious difference as to whether the tax should be levied on the land with or without improvements. The separate valuation of land and improvements in New York City has contributed interesting data in this field, and the most noteworthy discussion of the subject is to be found in the report in 1916 of the Mayor's Committee on Taxation. On this subject a majority of the Committee held that exclusive land taxes would tend to an intensive use of land in congested areas, which would be especially dangerous unless conditioned on a zoning system and limitation of building height, while the minority held that such exemption would tend to relieve urban congestion by promoting suburban development, and suggested as a compromise and test that the tax on building should gradually be reduced by 10 per cent yearly to half the rate on land.

The general property tax, comprehensive of all property, real and personal, tangible and intangible, which was the natural scheme for early taxation, has proved so unscientific and delusive in results as to be considered obsolete and objectionable in large measure by taxation authorities. It has never been, nor is it likely to be, a source for a federal revenue, and a trend of state legislation is already evident toward its replacement with respect to personal property by a classified property tax, in which tangible property only is directly taxed and intangibles are taxed by their income. The injustice of the former method, as in New York and Massachusetts, has been that so large a proportion of actual wealth has escaped disclosure that the tax upon the taxed portion has in many instances eaten up thirty or forty per cent of the income from many securities and left a net income far below minimum rates of interest. In respect to productive property the difference between a property tax and an income tax is chiefly one of proportion, and Professor Bullock has pointed out that the three-mill tax on intangible property in Minnesota is exactly the same as the six-per-cent income tax upon large incomes in Wisconsin. The wholesome trend of current legislation is toward the abandonment of the general property tax and its replacement by a classified property tax on land, improvements thereon, and moveable tangibles,

either at the same rates or at different rates, and by a personal income tax on incomes from intangibles and other sources—the first named tax exclusively for state and local purposes, the second dividing the field between the federal and state governments, preferably in such coördination as permits federal returns to be used as the basis of state taxation, without duplication of entry and return on the part of the taxpayer.

With respect to coördination of taxation within a state, the report of the Committee on a Model System of State and Local Taxation, of which Professor Charles J. Bullock of Harvard is chairman, presented to and approved by the National Tax Association at its meeting in November, 1918, presents a scheme well worthy of consideration. This proposes to recognize the threefold possibilities of tax levied, *i.e.* (1) at residence or domicile, (2) *in situ* or actual location, and (3) place of earning, by a threefold system, including (1) a personal income tax on all individual income levied at the taxpayer's residence, (2) a property tax on realty and other tangibles *in situ*, and (3) a tax on business or professional net earnings at the place where the business is located and the income earned. It is set forth that in this triple system each method of taxation would complement and cure defects in the other. In reply to the criticism that income from land and from a business or profession is again taxed to the individual as personal income, thus involving double taxation—which the Wisconsin law avoids by permitting taxes on personal property to be offset against the personal income tax—it is argued that this is not double taxation in the sense of being inequitable taxation, but simply obviates the need of a higher personal income tax, which would otherwise be required. The tax on business or profession, at the place of earning, covering alike individuals, firms and corporations, if adopted generally, would solve the question paramount in New York of obtaining from suburbanites residing in other states reasonable compensation for the facilities of earning, possible only in New York City, without the complication of deductions dependent upon taxation in other states, which the present New York tax law involves. The general scheme permits differentiation of rates in respect to land, improvements, and movable tangibles, or the omission of any tax on tangible personal property; also, the omission of the business or profession tax, especially in states which do not wish to tax non-residents. It may be added that the right of a state to tax non-residents with discrimination against them now waits decision by the United States Supreme Court in the case of the Yale & Towne Manufacturing Co.

Poll taxes are theoretically useful, not as a means of revenue, but because they identify even the humblest person, who pays no other direct taxes, with the operation of governments. But in practice they have been so subject to abuse that they have rightly fallen into disuse. They have, in fact, been made the indirect means of purchasing votes, by the practice of political parties to pay the poll tax for an individual vote, especially where such payment is a condition prerequisite to the right to the vote.

Taxes on sales are not recommended for use for any taxing unit, since they are peculiarly objectionable because they must be added to price at each sale, and thus increase in geometric proportion at each stage, as they finally fall upon the ultimate consumer. This objection, however, does not hold good on sales taxes imposed only once at the sale to the final consumer, which are not multiplied, but which are objectionable chiefly because of their inconvenience.

The use of stamps, as a means of sales tax, applied to the article itself or the document of transfer, also obviates this objection, and these have been the usual means of collecting taxes on tobacco in the first sale of the manufactured product. But as applied to other sales and to bank checks, etc., they are contrary to the methods and traditions of our people and of personal inconvenience, and have, therefore, been utilized almost entirely for unusual taxation during war periods.

Road taxes for the construction and maintenance of roads were originally purely local, because roads were chiefly used by those dwelling upon them and were consequently levied upon abutters and worked out in terms of "day's labor." The development of automobiles and the construction of national, state, and county roads as thoroughfares have changed all this, and the wear and tear upon roads is no longer from local vehicles, but from speeding automobiles and heavy motor trucks, which destroy roads, in direct proportion to weight and squared proportion to speed, according to the mathematical formula, mv^2, that impact is measured by mass multiplied by the square of velocity. In some states no licenses for drivers are required, while in others the requirements are rigid. Automobile permits are good only within the state, or by courtesy and with time restriction in other states, and there is no arrangement, such as existed between continental countries in Europe through the French triptych, for interstate travel. In traversing the Lincoln Highway from the Atlantic to the Pacific, the automobilist would pass through twelve states, requiring as many licenses, in case, as a traveler, he should desire to prolong his stay in the several states beyond the courtesy limits of time. Roadways have, in fact, like our railways and our waterways, become of interstate character, and to these are now added airways, even more of interstate extension. It would, therefore, seem proper that all who act as drivers or pilots on road or rail, on water or in air, should be equally made subject to examination and certification under license tax, either by federal authorities or under federal specifications, which would be uniform throughout the states. It may also be suggested that road taxes might be replaced by travel licenses for automobile vehicles varying with the weight and speed, *i.e.* horsepower of such vehicles, the collections to be made by federal authorities or under federal requirements and regulations, to be distributed in proportion to the mileage and width of good roads, respectively national, state and local, constructed and maintained to meet federal specifications, which licenses should be good throughout the states. It

is recognized that a chief need of the nation and of all localities is a thorough system of good roads, towards which this form of road licenses would be a direct help.

Summary

The Committee on Coördination in Taxation accordingly suggests the following as desiderata for wise coördination of taxes:

1. *Budgets:* National, state, and local budgets, with flexible and carefully safeguarded provision for contingencies, as a prime requisite for coördinated taxation.

2. *Federal Taxes:* In addition to (1) import or customs taxes reserved to the federal government and excise taxes of large return levied on the growth or manufacture of luxury products produced throughout the country, (2) a simplified form of progressive income tax levied on natural, if not on legal persons, and a graded business or corporation tax levied on corporations and other business concerns on profits, possibly with exemption of a normal per cent reckoned on the plant or property producing such profits, or on gross earnings or on dividends, in no case to exceed 50 per cent in the highest zone of either tax, as the preferable taxation in time of peace, omitting minor taxes of annoyance to individual taxpayers within adequate return to the government, levied under war conditions on the theory of finding every possible source of revenue. Possibly, also, inheritance taxes, on a flat basis, leaving graded taxes to state governments as now, or on a graded basis at least on intangibles, with partition of returns with the states, perhaps leaving to the states inheritance taxes on land and other tangibles, to be taxed *in situ*. Also, license fees for callings and transport agencies in national or interstate relations.

3. *State Taxes:* A tax system avoiding cross-taxation between the states on the lines of that recommended by the Committee of the National Tax Association on a Model System of State and Local Taxation, *i.e.:* (1) A classified property tax: on land, with or without a tax on other tangibles *in situ,* possibly with separate assessment of land and improvements, as well as movable tangibles, at different rates, as the basic revenue of the state, with the addition of local rates for local units; (2) A business or profession tax: on earnings within the state, also subject to local adjustment; (3) A general income tax: on residents at their place of residence, covering all sources of income—either additional and complementary to the other taxes, or made high enough to permit offset of the property and business taxes by deduction of their amounts—conforming as closely as practicable to the federal methods, and preferably a supertax imposed on the federal income tax. Possibly, also, inheritance taxes in coördination with federal inheritance taxes, if these be continued, and excluding tangible property elsewhere than in the state of residence; otherwise, on a graded basis and levied on residents to cover intangibles and tangible property within the state of residence. Also, license fees for professions or callings relating to public health or state jurisdiction and

requiring professional examination, as doctors, lawyers, and teachers, as well as those for automobile drivers and machines, if not included in federal taxes, issued under federal specifications and good throughout the states, with participation among taxing units, in proportion to good roads, state and local, conforming to national standards of construction and maintenance.

4. *Local Taxes:* Taxes superimposed upon or coördinated with state taxes on land and other tangibles and on business or professions within the local unit. Also, licenses on callings and transport facilities, involving tests of capability and police regulations, as horse drivers, trolley men, public conveyances, etc.

The purposes of this plan are to make taxation as simple and direct as practicable, avoiding cross taxation between the several taxing units, national, state, and local, and basing federal and state taxation, respectively, except as to personal income and corporation and inheritance taxes, on separate subjects of taxation, while permitting to localities provision for local needs by increased rates on land and property and business incomes. It seeks to avoid annoying and conflicting taxes in minor fields of taxation, which perplex and inconvenience the taxpayer without adequate return.[1]

THOMAS S. ADAMS,
LAWSON PURDY,
HENRY W. FARNAM,
R. R. BOWKER, *Chairman.*

December 29, 1919.

[1] Acknowledgment is made for the cordial coöperation and valuable help given by A. E. Holcomb, secretary of the National Tax Association, Professor Charles J. Bullock, chairman of its Committee on a Model System of State and Local Taxation, and Dr. C. C. Williamson, head of the Economics Department of the New York Public Library. It should be made clear that in this report, as is usual, all the individual points are not acceptable to every member, and that no one member, therefore, may rightly be quoted as accepting each individual position. The report, in a word, represents general approval and cannot be taken as the individual expression on each point of each member. Prof. H. L. Lutz of Oberlin College, though appointed on the Committee at its start, has not taken an active part in its work, and is, therefore, not a signer of the report.